UK Tax Bulletin

December 2014

Introduction

SQUIRE PATTON BOGGS

Latest Rates of Inflation and Interest

The following are the current rates at December 2014

Current Rates	December 2014
Retail Price Index: November 2014	257.1
Inflation Rate: November 2014	2.0%
Indexation factor from March 1982: to October 2014 to November 2014	 2.244 2.236

Interest on overdue tax

Interest on all unpaid tax is charged at the same rate.

The formula is Bank base rate plus 2.5% which gives a present rate of 3%.

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.5%.

Repayment supplement

Interest on all overpaid tax is payable at the same rate.

The formula is Bank base rate minus 1% but with an overriding minimum of 0.5% which applies at the present time.

Official rate of interest

To 6 April 2014: 4%

From 6 April 2014: 3.25%

Remittance Basis Charge

The announcement in the Autumn Statement that the non dom charge is going up to £90,000 for those who want to continue to access the remittance basis after they have been resident in the UK for 17 out of the last 20 years was a bit of a surprise. It sounds like a sensible linking up with the inheritance tax deemed domicile rules but unfortunately it isn't, when you think about it. It is also bound to cause confusion because the inheritance tax rules deem the individual to be UK domiciled whereas the non dom charge effectively confirms the non dom status of the individual.

What is worse, this proposal creates a huge anomaly.

Let us assume that a non dom individual who has been resident in the UK for a long time, leaves the UK and becomes non resident for 3 consecutive years and then resumes UK residence. On his return, he will not be liable to the £30,000 non dom charge because he will not have been UK resident for 7 out of the last 9 years; similarly he will not be liable for the £50,000 (soon to be £60,000) charge because he will not have been resident here for 12 out of the last 14 years. However, he will be liable to the £90,000 charge on the 17 out of 20 year rule. It is seriously upside down to suggest that somebody who has not been resident long enough to pay the entry level £30,000 charge will be stung for the £90,000 charge.

To be consistent with the non dom charge the test would be residence for 17 out of the last 19 years. That would make complete sense of the regime and although it would be out of kilter with the inheritance tax rule, that does not really matter. Inheritance tax is an entirely different tax with entirely different consequences and that differential gives rise to no anomaly or trap for the taxpayer.

Indeed it is no worse than the two entirely different methods of charging Stamp Duty Land Tax for residential and commercial property which are charged at different rates and on entirely different bases.

It remains to be seen how this ends up.

ATED

When I saw that the rates of ATED were going up by 50% above inflation I thought this meant an increase of about 4% as inflation was running at about 2.5%.

Silly me. What it means is that the rates are going up by 52.5%. Accordingly, for 2015 we now have the following tax charges:

- £2 million - £5 million : £23,350
- £5 million - £10 million : £54,450
- £10 million - £20 million - £109,050
- Over £20 million - £218,200

There is no indication of any change to the £7,000 charge to properties worth more than £1 million which comes into force next April so maybe that stays the same.

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Diverted Profits Tax

Hey - a new tax. As a tax adviser, that sounds like pretty good news. (Shame it is so bad for the country - but that's politics for you).

The idea is that next year, large companies will be subject to a new tax of 25% on profits which are artificially diverted from the UK. A similar charge will apply to foreign companies who have a UK turnover of more than £10 million but have artificially avoided having a permanent establishment in the UK.

I cannot even begin to explain. The rules are so imprecise that it would take all day. More importantly, the imprecision makes it virtually impossible for any taxpayer company to be able to determine whether or not they are liable to the tax, and how much the tax might be.

There is a responsibility on the taxpayer to determine whether or not they are potentially liable for this new tax - with a tax geared penalty for failing to do so. HMRC will then issue a notice for the tax which must be paid within 30 days. You would like to appeal? Dream on. There is no right of appeal nor any right to postpone the tax.

This is obviously extremely serious so it is inevitable that your friendly tax adviser is going to be heavily involved in all these issues.

A very important feature is that this tax may not be covered by double taxation agreements because most treaties apply to "identical or substantially similar taxes" to income tax, corporation tax and capital gains tax.

It is by no means clear that the Diverted Profits Tax will be an identical or substantially similar tax - but whether it is or not, some interesting possibilities arise. Let us assume that a UK company within the scope of the new tax has diverted profits to (say) Belgerland where the rate of corporation tax is 15%. If the diverted profits tax is not substantially similar to the main UK taxes then no credit will be allowed against the Belgerland corporation tax and the company will end up paying 15% in Belgerland and 25% in the UK on the same profit. This would obviously be intolerable and probably lead to a withdrawal of business activity in Belgerland.

However, if the diverted profits tax is found to be substantially similar to UK corporation tax then the result will be that the UK tax may eliminate the Belgerland tax liability and the whole of the company tax liability will be payable to the UK. The Belgerland Government would no doubt rejoice that the UK are taking such a firm stand against tax avoidance. Or maybe not. Perhaps they would enquire why the UK is pinching their tax revenue.

Some people might wonder whether this new tax achieves anything more than the present rules on transfer pricing and the attribution of profits to a UK Permanent Establishment. (And what about the GAAR - would not that deal with any such artificial arrangements.)

Of course, the new tax will apply where there is no PE. That's a bit curious too. We have lots of double taxation agreements which say that foreign companies can only be taxed here on the profits attributable to a PE. So now we will tax them whether there is a PE or not. I guess our treaty (and EU) partners will have a view on this.

I expect that these proposals will provoke a degree of discussion and possibly some modification before the proposed tax comes into force on 1 April 2015.

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Goodwill on Incorporation

For some time, HMRC have been considering the position where a professional person incorporates his business. Their view was that a company cannot carry on a profession and therefore it was impossible to transfer a professional activity to a company. Furthermore, they say that the goodwill resides in the professional person and that cannot be transferred to his company either.

This resulted in one interesting letter from HMRC in which they expressed the firm view that corporation tax cannot apply to profits from a profession with the (rather unlikely) result that the company's profits would presumably be tax free – a view which I'm sure was a surprise to the Law Society, the Institute of Chartered Accountants, the RIBA, the RICS and others.

However, HMRC seem to have concluded their review and now accept that a professional activity can be transferred to a company – and so can the goodwill.

It is perhaps a coincidence that this change of view arises just at the time when HMRC have decided to remove entitlement to CGT entrepreneurs relief for such transfers, and to eliminate any corporation tax deduction for the goodwill value for the company.

Anyway, whatever the motivation, things now seem to be clearer and the issues will be whether there has been a valid transfer of the business to the company and whether the goodwill has been properly valued.

Even without entrepreneurs relief, the capital gains tax treatment still gives rise to a considerable advantage and HMRC remain vigilant about the possibility of the goodwill being transferred at an over value. As long ago as April 2005 they published a detailed statement explaining that where the amount paid for goodwill is excessive, it will be treated either as a distribution or as earnings – although with the possibility of remedial action (such as a repayment to the company of any over value) as an alternative.

The provisions of Section 774 Income Tax Act 2007 should not be overlooked in this context because they apply to capital sums received from the exploitation of the earning capacity of an individual from a profession or vocation – which HMRC suggest covers entertainers, pop stars and sportsmen. In such cases, any capital sum would be chargeable to income tax under Section 776 so the changes to entrepreneurs relief would not have any effect anyway.

Inheritance Tax : Multiple Trusts

HMRC have announced that they have abandoned the idea of a single nil rate band for trusts, but have decided to make changes to limit the advantages of multiple trusts – mainly by ensuring that where property is added to two or more settlements on the same day they will be aggregated for the purpose of calculating the trusts charges to inheritance tax.

The idea is that the initial value of the property together with the property added later will be brought into the calculations for the 10 year charges and the exit charges. It will apply to trusts created on or after 10 December 2014 and will also apply to earlier trusts where property is added later.

In another change, HMRC propose to amend the definition of a qualifying interest in possession where a spouse succeeds to a life interest to which their spouse was previously entitled. Where the interest is not a transitional serial interest Section 80 IHTA 1984 will apply to treat a new settlement as having been made on that occasion so that the property can thereafter be subject to the relevant property charges.

A further, and very welcome, change is to be made to the calculation of the 10 year and exit charges arising after 6 April 2015. The calculation is to be made without regard to the existence of excluded property and this will simplify matters (and avoid a significant trap) for trustees.

I am conscious that the above paragraphs probably mean absolutely nothing to anybody who is not up to his eyeballs in related property and excluded property settlements. For others it will be REALLY interesting. I think I should get out more.

Happy Christmas

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